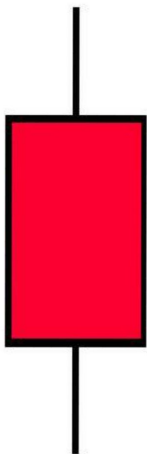


VISIT...

LANZAROTE
Caliente.COM

MATT LEROUGE



**STOP
LOSSES**

STOP LOSSES

*The art of stopping losses
must be mastered
before profits can be
taken.*

**An invaluable guide on
HOW TO STOP YOUR
TRADING LOSSES**

Whether you're just starting out or you're a seasoned trader, this set of concise rules, explanations, examples, and solutions will serve as both vital warnings and reminders to guard against the myriad pitfalls facing every trader.

**Matt
LeRouge
is an avid
day
trader
who has
experienced
all the
euphoric**

**highs and
appalling
lows
imaginable
in his five
years of
trading
stocks,
currency
pairs, and
CFDs.**

Copyright © Matt LeRouge 2013

Rule 1: Your Stop Loss must be less than your Take Profit

Explanation: Never risk more than you could potentially gain in any single trade.

Analysis: Amateur trading systems often incorporate Stop Losses that are many times larger than their Take Profit target, based on the erroneous belief that this will allow them to ride out price swings. While this may work in some cases, it won't every time and ruinous losses will

rapidly be accrued.





Example 1: Jon uses a system with a 10 point Take Profit and a 20 point Stop Loss and makes ten trades over a couple of days. He enters trades carefully when he feels that there's a higher probability of success and is pleased when 50% of them reach his Take Profit – allowing him to pocket 50 points (10 points x 5). The trouble is that he hits his Stop Loss five times too, losing 100 points (5 x 20 points). Despite his 50% success rate, the result of his ten trades is a loss of 50 points.



Example 2: Geoff uses a 20 point Take Profit and a 10 point Stop Loss. Over ten trades he also has a 50% success rate, but as his Stop Loss is half his Take Profit, his results are far better than Jon's. Geoff pockets 100 points (5 x 20 points) from his successful trades, but only loses 50 points (5 x 10 points), so the result is a healthy profit of 50 points.



Solution: As a rule of thumb, always ensure that your Stop Loss is at least half the size of your Take Profit.

Rule 2: Don't knock the Demo





Explanation: Never trade with real money until you're absolutely confident of your skills.

Analysis: This is a crucial lesson that too many new traders fail to learn. It may seem more exciting and realistic,

but losing real money is expensive. Take advantage of all the free demos on offer and do what used to be called ‘paper trading’ – use a demo account to place trades in real time without risking your capital. Stick with the demo account for as long as possible to gauge your progress. Save your hard-earned cash until you’re sure you can succeed consistently.

Example: John convinced himself that the only way to understand the true nature of trading was to use real money. Geoff, on the other hand, felt sure that he’d learn more with a demo account. After a week of trading real cash, John had seen gains of several hundred

pounds at times, but his overall result for the week was minus £375. Geoff also fared poorly during the same week and ended up with an imaginary loss of £480.



John was horrified by his losses, but concluded that, having experienced real money trading, he had gained valuable trading experience. He also realized that the only way to recoup his £375 was to continue trading with real money the following week. Needless to say, his desperation to recoup his losses had been partially to blame for his poor trading that week and his decision to

continue was a recipe for financial disaster.

Geoff was disappointed by his sizable imaginary loss, yet he felt that he had learned a lot from his week of experience and he also resolved to continue trading the following week. His motivation, however, was very different to John's: rather than being determined to recoup his losses, Geoff planned to further develop his skills by practicing within the demo platform and felt under no pressure to rush.

Solution: Treat demo trading just as if

it were real money trading. Only by following strict rules and keeping accurate records ([see Rule 6](#)) will you be able to monitor your trading development effectively.

Rule 3: Learn from mistakes and Be ready to admit failure

Explanation: If you've made a mistake, analyze what happened – *be honest* – was it human error or platform error? Platform errors are frequent enough, but human error, usually the result of uncontrolled emotional responses, is most often to blame. Get out of trading altogether if you're consistently losing, don't keep coming back for more losses.

Analysis: It's all too easy to write off losses as bad luck, platform error, or inexperience and reason that next time your luck will improve, the platform will function smoothly, and you'll have accumulated enough experience to reap rewards. What's much harder, and almost impossible for many new traders, is to accept that you alone are entirely responsible for your losses.



Example: John starts the day with £500 in his trading account and has reduced his balance to £150 within an

hour due to several poorly executed trades. Rather than accepting his bad trades and calling it a day, he is determined to both recoup his losses and make a profit that day and proceeds to enter more trades with increasingly bad judgment that's skewed by his irrational desire to recoup losses and has broken [Rule 4](#) in the process. He soon emptied his trading account and replenishes it with another £500 that rapidly disappears in the same fashion.



Solution: Understand your mistakes and, if you can't help repeating them, be ready to admit that you're failing. Set yourself a strict loss limit at which point

you stop trading and either get out or switch back to a Demo account ([see Rule 2](#)).

Rule 4: Never gamble

Explanation: Don't apply a gambler's attitude – trading is not about going either way with a 50/50 chance of winning.



Analysis: Although trading *is* essentially a choice between buying or selling, it is worlds away from roulette and should never be approached with an attitude of luck. Having ‘a feeling’ that something is about to happen should not be confused with understanding why you feel that something may be about to happen.

Ignorant traders or those reduced to desperation by heavy losses who resort, almost literally, to a toss of the coin may as well visit a casino instead. If you ever feel that your trading is drifting towards an attitude of hope and gambling – STOP, take some time out and your losses will stop too.



Example: After reading a negative article about Facebook in the financial press, John had a quick look at the Facebook daily chart and convinced himself that a downturn was imminent. Not wanting to miss out on what he felt certain would be a sudden drop in share

price, he immediately sold a large number of Facebook CFDs. He then waited for the share to start its downward trend but, instead, it simply ranged for the rest of the day, closing slightly higher at the close of trading.



Geoff had read the same article about Facebook and also felt that it might indicate a potential trade. However, rather than rush into a position as John had done, he spent the rest of the day checking various price levels that Facebook had previously traded at and analyzing chart patterns and trading volumes over various time frames in order to gauge as best as he could the

probability of a future drop in share price. He eventually concluded that, if the price dropped below a certain level, it would indicate a definite weakness of the stock and an ideal entry point for a sell. Two days later Facebook fell to the level that Geoff had marked and he sold the stock through his Demo account. His analysis proved correct and he netted a good (imaginary) profit on the trade. By this time John had long since closed his Facebook position for a loss and had lost interest in Facebook shares altogether.



Solution: You must only trade when

there's a high probability of the trade succeeding.

Rule 5: Ignore the hype

Explanation: You won't make your fortune overnight. Be patient and persistent – hard work will pay off.



Analysis: It looks like easy money –

where else, apart from casinos, can you earn thousands in just a few minutes or even seconds? Trading shares or CFDs is the answer, but it's also the answer to a similar question – where else, apart from casinos, can you *lose* thousands in just a few minutes or even seconds?



Example: On the day that John started working from home as a day trader using a cash trading account, he dressed up in a smart suit much like he imagined professional traders wore and he let everyone know about his new career and the substantial rewards he would inevitably reap.



As you can probably guess, Geoff did no such thing. He started gradually with realistic expectations having thoroughly investigated the world of trading before opening his Demo trading account.



Solution: Ignore the alluring promises of trading platforms, self-help books, and Youtube videos. Take your time, think long term, and don't be blinded by thoughts of instant riches.

Rule 6: Keep a record of progress and Go easy on the ego (however difficult this may be)



Explanation: The general non-trading public tends to be a little overawed by anyone involved in trading, so it's easy to start strutting about and playing the role of a successful trader. But the more you strut, the harder it becomes to admit

to yourself and others if you're failing and the bluster becomes a desperate defence that will ultimately ruin you. Many traders keep lying to themselves until the very end, mentally inflating their profits and shrinking their losses.

Analysis: Just as we have the ability to forget physical pain, we also have the capacity to forget the mental pain of a trade gone wrong. Our minds will do a great job of burying upsetting memories of bad trades beneath whatever positive news can be gleaned from the day, however insubstantial it may be.



Example: One day Jon makes five trades, each with a Stop Loss of 20 points and a Take Profit of 40 points. Of these, one starts off well and he manages to zero his stop loss before the position reverses and stops him out. He's ecstatic when another of the trades hits his Take Profit and he closes for 40 points profit, but his mood sours when the other three trades hit his Stop Loss. He loses 60 points and ends up with a total of minus 20 points for the day.

Despite having had a bad day, however, Jon focuses on the thrill he felt at hitting

his Take Profit and, by the time he meets his girlfriend that evening, he has almost forgotten about his losses and instead tells her about his successful trade and waxes lyrical about how bright the future is. Any doubtful questions from his girlfriend are brushed off just as he dismisses any doubts that occur within his own mind.



Solution: Accurate records will allow you to realistically assess your progress. Admit errors to yourself and, crucially, to others – talk openly to your friends, fellow traders, and family about how you're really doing.

Rule 7: Stick with your system.

Explanation: Develop your system and stick with it until it's thoroughly tested. Make adjustments, but allow time to assess them before any changes are made.

Analysis: Without a system you'll be trading in the dark. Systems can be as complex or simple as you like, but you must have a system of some description in place. All systems need time to prove themselves so, although minor

adjustments can be made along the way,
avoid dropping your system entirely
after just one or two bad experiences.



Example: Having noticed what appeared to be a regular pattern linked

to the opening levels of the FTSE index, John developed a system whereby he only placed a trade if the FTSE exceeded its first five minute candle within the first fifteen minutes of trading. The system had potential, but John's impatience meant that he changed his parameters on an almost daily basis and so never actually tested each set of parameters more than once.



Solution: Give any system at least a week's trial. Demo accounts ([see Rule 2](#)) are by far the best way to test a system – multiple systems can be tested simultaneously using several free Demo accounts.

Rule 8: Never rely on indicators

Explanation: Indicators do are nothing more than indicate. Like weather vanes, they show the right direction once strong winds are blowing, but not before. Indicators cannot provide information about what will happen next.

Analysis: Every trading platform offers a bewildering range of indicators that can be applied to charts to provide an *indication* of movement or impending price reversals. Many promises have

been made about how these indicators can predict movement, but it's simply not possible for them to do so. **Moving Averages, Stochastics, MACD, and Bollinger Bands** are among the most popular indicators and all are the product of historical information, whether it be from the past few hours, days, or years. From this information they give an indication of whether specific stocks or indices are 'overbought' or 'oversold' ie. Whether it's likely that a price has climbed or fallen as high or low as is possible and a reversal is imminent. But, as any experienced trader knows, there is no such thing as a rock solid bottom or top for prices ([see Rule 9](#)).



Example 1: Jon follows a common system based on entering or exiting a trade whenever a short **Moving Average** indicator crosses a longer Moving Average indicator based on the assumption that this tends to indicate a change in direction. Though it proves successful on several occasions, more often than not Jon finds that it's rarely as simple as it looks. The Moving Average lines frequently reverse their crossovers

almost immediately or remain indecisive as prices stagnate. Jon eventually comes to the conclusion that his system is doomed to failure. **MACD** (Moving Average Connvergence/Divergence) is a development of the Moving Average system that Jon tried and is likely to find just as (in)effective.



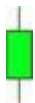
Example 2: Geoff keeps a close eye on **Stochastics**, which indicates whether a stock or index is overbought or oversold and, when it does so, Geoff

enters a trade in the opposite direction and awaits the price reversal that will net him profits. Though this works in his favour several times, Geoff is perplexed when he realizes that the stock frequently continues rising or falling way beyond what Stochastics indicates. At such times the Stochastic indicator simply bottoms or tops out and is rendered useless. Geoff has to sit back and watch as his Stop Loss is hit time and time again. If he's not careful, he'll be in danger of breaking [Rule 9](#).



Example 3: John uses **Bollinger Bands** as indications of when to enter or exit a trade. Named after its creator John Bollinger, the indicator consists of an upper and lower band limit to a price. Once the price of a stock touches the lower band, John buys and, when it touches the upper band, he sells in the expectation of a price reversal. This works well a few times and so he continues to follow his system, but comes unstuck when the stock price

begins to 'walk the Bollinger band'- rather than reverse when it touches the lower band, the stock price continues to fall and the Bollinger Band simply falls with it. To his acute disappointment he has to stomach repeated losses, many of which could have been prevented if he'd followed [Rule 9](#).



Solution: Use indicators for nothing more than what their name suggests: *Indication*.

Rule 9: Don't catch a falling knife

Explanation: Attempting to predict the bottom of a rapidly dropping share with the hope of buying at the moment of reversal is an elementary blunder that can and will wipe out your account in minutes.

Analysis: It's unusual for whatever you're trading to reverse immediately after a sharp fall, in most cases further falls are likely before the actual reversal

occurs and it's from these successive drops that the phrase 'catching a falling knife' derives. It is, however, true that sharp falls are often followed by reversals that 'correct' the sudden dip, so it is worth monitoring such movements, but hasty entries should be avoided ([see Rule 4](#)).



Example: Following unexpectedly poor US unemployment data, John observes the FTSE index plunge over 50 points in just a few seconds. When the index's downward momentum pauses,

John jumps in with a Buy, convinced that he's caught the point of reversal and is about to net a good 50 points as the index corrects itself. But things don't go to John's plan and, after treading water for a few more moments, the FTSE index plunges another 20 points, blitzing John's Stop Loss in the process. Unperturbed, he readies himself for what he believes must surely be the actual reversal – and, when a strong green candle flicks upwards, he jumps in again with a Buy, only to be wiped out once more as the index continues its downward fall. Desperate to recoup his losses, John has another couple of attempts and fails both times. The index does eventually reverse and makes up

most of the lost ground, but by that time John has lost more than he can stomach and has belatedly signed out of his account for the day.





Solution: Be patient. Wait for genuine signs of a reversal such as a consolidation of prices at a particular level, and repeated unsuccessful attempts to fall further.

Rule 10: DIY

Explanation: Don't bother buying robots (Bots) or following trading tips, use your own brain – a robot trader will never be as effective as you and will frequently make ruinous trades that a human would never have entered.

Analysis: A quick internet search will turn up hundreds of offers for trading Bots with promises of quick and reliable returns. These are, without exception, simple programs with pre-set parameters linked to any number of the

indicators discussed in [Rule 8](#) which will automatically trigger trades through your trading platform. While some Bots may boast an impressive history, it's vital to understand that, just like the indicators they rely upon, Bots have no capacity to predict the future and will frequently make disastrous trades based on historic analysis.



Example: Disappointed with his own trading results, Jon decides to invest in a Bot that has an impressive history and promises more of the same. Initial

results are promising, but, after a week, reversals have brought his balance back to zero. The same pattern occurs the following week and the week after. Perplexed by these results, Jon analyses the charts and realizes that the currency pair the Bot has been trading is locked into a channel. It has simply been trending in a horizontal zigzag for weeks. He decides to wait for the channel to be broken in the hope that the Bot will capitalize on the opportunity. By chance, the channel breaks the very next day, but, to his horror, he sees that the Bot has opened multiple trades in the opposite direction to the new trend and is hemorrhaging cash from his account. He takes emergency action and closes

all the trades manually, taking a significant loss in the process. What was blatantly obvious to the human eye was invisible to the Bot.





Solution: Fine-tune your own trading systems instead ([see Rule 7](#)).

Rule 11: Don't be a forum-follower

Explanation: The web is packed with forums devoted to all aspects of trading and these are often the first port of call for exasperated amateurs. While there's plenty of good advice and support out there, be very wary about members praising or criticizing particular stocks.

Analysis: However convincing a member's belief in the fortunes of a particular stock may be, their only interest is to talk up or down the prices

of the shares they've bought or sold. Many traders make a living from doing just this: Buying or selling a stock and then spending days and weeks using their multiple forum aliases to post about the stock in an attempt to 'pump' or 'dump' its price before selling or buying at a profit.



Example: John's so disappointed by his recent losses that he starts cruising stock forums in the hope of gleaning tips about a stock that's just about to rocket. He soon finds a forum whose members are raving about a penny tech stock called PocketBurner that's trading at just a few pence and is bound to go ballistic after its earnings

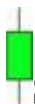
are announced next week. John gets excited too and buys ten thousand shares at 5p each. He posts his trade on the forum and is rewarded with a bunch of replies congratulating him on his good sense. The next day he's overjoyed to see that PocketBurner has risen by half a penny and so decides to buy ten thousand more shares at 5.5p. Meanwhile the forum members, who he now follows closely, continue to bang on about the share so that by the end of the day he's convinced himself into buying ten thousand more shares which, by this time, have risen to 6p. Three days later, the day before PocketBurner's earnings are announced, John is sitting on 50,000 shares that he bought in batches of

10,000 each time the price increased by half a penny – a total investment of £3000. That afternoon John is horrified to see the price drop sharply from 7p to 5p and, when he desperately scans the forum for an explanation, is relieved to find its members unconcerned and recommending further buys at this lower price. John checks his bank account before piling in with a purchase of 50,000 shares at 5p, confident that he'll be massively rewarded the following day and even bragging to his friends about his good fortune. Half an hour before the market closes, he watches distraught as the price fails to rise above 5p and instead falls to 4p, then 3.5p, before settling at 3p as the market

closes. John's 100,000 shares that cost him £5500 are now worth just £3000. After a sleepless night, John sits at his computer awaiting the promised good earnings news that will save him, but nothing materializes and PocketBurner's share price drops a further penny. He notices that the usually buzzing forum has gone strangely quiet. He finally offloads his 100,000 shares later that afternoon at 1.5p each for a gut-wrenching loss of £4000.

He later learns that PocketBurner had been 'pumped and dumped' by unscrupulous traders preying on the naivety of new traders. They had bought in early, 'pumped' the stock with fantastic tales of its future, and then

‘dumped’ it for massive profits shortly before the supposed good news that failed to materialize.



Solution: Use forums to socialize with fellow traders and perhaps pick up general trading advice, but be extremely wary of any ‘hot tips’.

Rule 12: Know the news

Explanation: Economic news is released throughout the year at regular, scheduled times.

Analysis: Although many are insignificant and have a negligible impact on the markets, there are plenty of economic news items such as the monthly US Unemployment Rate and the Bank of England's monthly Rate Decision that have the potential to jerk the market vigorously in unpredictable directions.



Example: John noticed that the FTSE was rising steadily early one afternoon and decided to buy into the index. He got a good entry and, for an hour or so, his position did well but at exactly 2.30pm the index plummeted unexpectedly and his profits along with his Stop Loss were wiped out in seconds. Somewhat bewildered, he belatedly checked the economic calendar and discovered to his horror that he had placed his trade an hour before the UK GDP estimate had been announced – the forecast had been positive, hence the earlier steady rise, but the actual figure triggered an immediate drop across the markets as it

was way below expectations.



Solution: Always keep an eye on any of the economic calendars that can be found for free online and which provide an indication of the impact each news item is likely to have on the market. Never enter trades without checking which numbers are due for release that day.



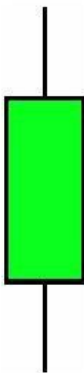
Rule 13: Buy *Take Profits* by *Matt LeRouge*

Explanation: *Matt LeRouge* outlines his winning trading strategies in *Take Profits*.



Example:

TAKE PROFITS



Matt LeRouge



Solution: Buy a copy of *Take Profits*.

Table of Contents

STOP LOSSES

Rule 1: Your Stop Loss must be less than
your Take Profit

Rule 2: Don't knock the Demo

Rule 3: Learn from mistakes and Be
ready to admit failure

Rule 4: Never gamble

Rule 5: Ignore the hype

Rule 6: Keep a record of progress and
Go easy on the ego (however difficult
this may be)

Rule 7: Stick with your system.

Rule 8: Never rely on indicators

Rule 9: Don't catch a falling knife

Rule 10: DIY

Rule 11: Don't be a forum-follower

Rule 12: Know the news

Rule 13: Buy Take Profits by Matt
LeRouge